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Supreme Court of the United States

OCTOBER TERM, 1959

No. 374

HAYS, ST. JOHN, ABRAMSON & HEILBRON,

Petitioners,

against

EDWARD M. GARLOCK and SURFACE TRANSIT, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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To the Chief Justice of the United States and the Associate Justices of the United States Supreme Court:

Petitioners respectfully ask this Court to issue a writ of certiorari to review the final order of the Court of Appeals for the Second Circuit which affirmed (with a modification) an order of the District Court for the Southern District of New York dividing allowances in reorganization proceedings between petitioners and the individual respondent.

The Opinion Below

The opinion of the District Court is not reported; the opinion of the Court of Appeals is reported at 266 F. 2d 862. Copies of both have been supplied by petitioners Rosner and Saxe, Bacon & O'Shea.

The Grounds of Jurisdiction

(i) The judgment sought to be reviewed was dated and entered on May 11, 1959.

(ii) Timely application for rehearing was denied on June 10, 1959.

(iii) Jurisdiction of this Court is invoked under 28 U. S. C. § 1254(1).

Questions Presented for Review

1. May a District Court, in awarding allowances in a Chapter X proceeding under the Bankruptcy Act, make separate allowances to the attorneys for the petitioning creditors and to counsel associated with them?

2. Where a firm of attorneys and a single practitioner about to institute an Article X proceeding under the Bankruptcy Act agree to make an equal division of fees in the expectation that they would share equally in the work and the firm and the individual both have performed extensive and valuable services, can the District Court weigh the relative amount of services performed by each?

3. Where the Securities and Exchange Commission has, in a Chapter X proceeding under the Bankruptcy Act with which one of its representatives has been continuously familiar, recommended a certain division of compensation among attorneys, may the District Court disregard that recommendation when the proceedings were originally conducted before a different judge?

4. Is the administration of a Chapter X proceeding under the Bankruptcy Act facilitated when an individual practitioner who was unwilling to institute the proceeding without participation by a firm of attorneys receives an allowance of $132,500 and the firm only $10,000, when ex-

tensive and valuable services were performed by the firm in addition to the overhead necessarily involved in the firm's acting as attorneys for the petitioning creditors?

Statutes Involved

11 U. S. C. 102:

"(c) A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, rendering services in a proceeding under this title or in connection with such proceeding, shall not in any form or guise share or agree to share his compensation for such services with any person not contributing thereto, or share or agree to share in the compensation of any person rendering services in a proceeding under this title or in connection with such proceeding, to which services he has not contributed: *Provided, however,* That an attorney-at-law may share such compensation with a law partner or with a forwarding attorney-at-law, and may share in the compensation of a law partner.

(d) A receiver or trustee or the attorney for any of them, or any other attorney, seeking compensation for services rendered by him in a proceeding under this title or in connection with such proceeding, shall file with the court his petition setting forth the value and extent of the services rendered, the amount requested, and what allowances, if any, have theretofore been made to him. Such petition shall be accompanied by his affidavit stating whether an agreement or understanding exists between the petitioner and any other person for a division of compensation and, if so, the nature and particulars thereof. If satisfied that the petitioner has, in any form or guise, shared or agreed to share his compensation or in the compenstion of any other person contrary to the provisions of subdivision (c) of this section, the court shall withhold all compensation from such petitioner."

11 U. S. C. 641:

"§ 641. PETITIONING CREDITORS; COURT OFFICERS; ATTORNEYS THEREFOR

The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceeding under this chapter—

• • •

(5) by the attorney for the petitioning creditors."

11 U. S. C. 649:

"§ 649. STATEMENT OF CLAIMS OR STOCK ACQUIRED OR TRANSFERRED AFTER COMMENCEMENT OF PROCEEDING

Any persons seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred."

Statement of the Case

In October 1948 a petition for the reorganization of the Third Avenue Transit system in the City of New York was filed under Chapter X of the Bankruptcy Act. The

instant petitioners were, together with one Robert Irving Lennox, since deceased, the attorneys for the petitioning creditors. They had entered into an oral agreement with the individual respondent, Edward M. Garlock, which contemplated a division of the compensation to which they might become entitled in the following proportions: 20% to Lennox, 40% to Garlock, 40% to Hays firm. Garlock, from the beginning, acted as chief counsel. On behalf of the firm the principal services were performed by Arthur Garfield Hays and Osmond K. Fraenkel. Mr. Lennox died in 1953. The corporate respondent is the reorganized company.

The application was bitterly contested by the Third Avenue interests until June 1949, when they capitulated. Thereafter, various important matters were litigated, two of which reached the Court of Appeals. In the first of these the petitioning creditors alone took the appeal, the successful outcome of which was of great benefit to the estate; in the second, the petitioning creditors were among those actively participating on the successful side. The attorneys for the petitioning creditors also performed extensive and valuable services in connection with the various plans proposed and the one ultimately approved.

The final plan provided for the acquisition of the Third Avenue system by the Fifth Avenue Coach system. It was very successful. The senior bondholders, among whom were the petitioning creditors, were paid in full. The junior bondholders received a substantial return on their investment.

After the consummation of the plan numerous persons applied for allowances. Extensive hearings were held before Judge Dimock. Originally a petition was filed by the Hays firm for an allowance of $325,000 for the services performed by it as attorneys for the petitioning creditors and by Mr. Garlock as counsel. Then Mr. Garlock filed an independent application asking for $300,000 for himself alone. A sepa-

rate petition was also filed by the Lennox estate, claiming $75,000. At the hearings before Judge Dimock the firm contended that under the relevant provision of Chapter X (11 U. S. C. 641, sub. 5) only the "attorney" for the petitioning creditors is entitled to compensation. Such a construction of the statute would, the firm urged, obviate the necessity for considering whether certain assignments made by Mr. Garlock (many as security for debts; one outright to a trustee for the benefit of his wife) violated Section 649 of Title 11 and Section 102, subds. c and d.

The firm contended that, in any event, since the firm had performed extensive and valuable services the Court had no power to make a division other than that which had been agreed upon by the firm and Garlock and that it would be a disservice to the administration of Chapter X proceedings to make the division depend on the relative quanta of services performed. This, it was urged, would result, during the proceedings, in rivalry and self-glorification where cooperation and submerging of personalities should be the rule.

At the hearings the SEC recommended allowances of $30,000 to the firm, $115,000 to Mr. Garlock, and $7,500 to the Lennox estate. Judge Dimock reduced the allowance to the firm to $10,000, increased Garlock's to $150,000, and awarded the Lennox estate what the SEC had recommended. The court below upheld the reduction to the firm and part of the increase to Garlock, cutting that to $132,500; but reduced the Lennox estate to $2,500.

In its opinion the court below entirely ignored the arguments made by the firm. As pointed out in the application for rehearing the court apparently misunderstood the situation. We shall, therefore, describe the relation between the parties and the respective services performed by the firm and Mr. Garlock as briefly as possible.

1. Before these proceedings were instituted Mr. Garlock had been involved in litigation arising out of the way the Third Avenue Transit system was operated and had acquired extensive information concerning its affairs. One of his clients, Aaron Melnicker, had discussed with him the feasibility of instituting a Chapter X proceeding. In the Fall of 1948 Mr. Garlock prepared a petition which it was expected Mr. Melnicker, one of his brothers and a third person would sign. It had been expected that a law firm which represented that third person would participate. But when that person withdrew for reasons of health, Mr. Garlock told Mr. Melnicker that he would not go ahead unless a law firm with adequate facilities would join. Mr. Melnicker then suggested the Hays firm and they agreed to become attorneys of record on the allowance-sharing basis already mentioned. Mr. Lennox was added as co-attorney because he was an office associate of Mr. Melnicker.

2. The filing of the petition in October 1948 stirred up a hornet's nest. The debtor and others moved to dismiss and unsuccessfully resisted petitioners' application to amend. After this application was granted and the petition amended attacks on it continued. Numerous legal objections were raised which required legal research and the filing of briefs. The chief attack was on the good faith of the petitioners—the debtor claiming that there had been improper solicitation in the selection of the third petitioner. Hearings on this issue were held in the Spring of 1949 before Judge Samuel Kaufman. He finally ruled that he could not determine that issue without proof with respect to the insolvency of the company and sent that issue to a referee. Before any hearings were ever scheduled before the referee the company surrendered and admitted its insolvency. Accordingly, in June 1949 Judge Kaufman entered an order approving the petition.

During this nine months period of intense activity, both in and out of court, the firm actively participated in every-

thing which occurred. Mr. Garlock, who was the expert and who had planned the case was retained as counsel. Naturally he expected to conduct the case in his own way. But he was continuously assisted by the firm, particularly by Mr. Arthur Garfield Hays and Mr. Osmond K. Fraenkel, who was associated with the Hays firm. They appeared in court on numerous occasions, researched and wrote most of the briefs, and were at all times ready with support and advice (see Supplemental application, pp. 7-11, S.M. 2617-21, *infra*, pp. 3a-5a).

3. After the petition was allowed there followed a period of inactivity. However, in the Spring of 1950 a very important issue arose in the administration of the estate. The reorganization trustees needed cash. They looked with longing at the cash in the hands of the trustee under the first mortgage and persuaded the court to direct a compulsory loan. This had been objected to by various of the parties in interest, including the petitioning creditors. But the petitioning creditors alone prosecuted the appeal from that order (see 198 F. 2d 703). The importance of the result achieved has been recognized by everyone connected with the case (see Surface App. p. 51).

Mr. Garlock claims sole credit for what was here accomplished. We would be the last to suggest that he is not entitled to great credit. But throughout that fight the resources of the firm were available to him and were used by him. Mr. Fraenkel participated in many of the discussions with Judge Kaufman and in the work necessary to get the record docketed and the appendices prepared (see Application, pp. 12-15; S.M. 26740-42, *infra*, pp. 10a-12a). Mr. Garlock claims that he wrote the brief without help; Mr. Fraenkel testified that he drafted a small part of it (S.M. 26741). Mr. Fraenkel would, of course, have been willing to write the brief and argue the appeal himself (his

ability to do which could not be questioned), but it did not occur to him to suggest supplanting Mr. Garlock on this or any other occasion.

4. In connection with the Plan hearings an issue arose with regard to the status of certain treasury bonds. Messrs. Hays and Fraenkel assisted Mr. Garlock at the hearings on this issue. No doubt here again Mr. Garlock, as had been expected, conducted the examination of witnesses. He also, with some help from Mr. Fraenkel, participated in the appeal prosecuted by the indenture trustee, again resulting in a favorable decision (222 F. 2d 466) (see Application, pp. 16-19).

During all this time the firm's loyalty to Mr. Garlock was steadfast (see 26722-5, 26811, 12, 26827, *infra*, pp. 5a-8a, 12a-13a). Mr. Hays emphatically rejected Mr. Lennox's suggestion (motivated in part by the hope of increasing his share of any compensation) that Mr. Garlock be replaced (S.M. 26722-4, 26766). And when serious objection was raised to the prosecution of the compulsory loan appeal, Mr. Hays again supported Mr. Garlock (S.M. 26724, 25). Indeed, at no time has Mr. Garlock suggested that he was not faithfully supported. Mr. Garlock testified that at no time did he ask Mr. Fraenkel to do anything in the matter which he failed or refused to do (S.M. 26309). And, with respect to Messrs. Hays and Heilbron, he gave the same testimony, adding "I just hardly ever wanted to see them" (S.M. 26315). And Mr. Fraenkel testified that the firm tried to oblige Mr. Garlock whenever he asked for help, but this happened oftener in the beginning than later (S.M. 26847; see also 26860, 26871). "We tried to perform as a team" (S.M. 26861).

During the course of the proceedings Mr. Melnicker looked to the firm to represent his interests and keep him informed (S.M. 26725-29, *infra*, pp. 7a-10a). At one time he requested, in a letter, that only Messrs. Hays, Heilbron

or Fraenkel actually appear in court (S.M. 26726, 27, Hays Exhibit 1 as of 4/1/58). Mr. Fraenkel persuaded him that Mr. Garlock should continue to act in Court (S.M. p. 26726).

It was not until the commencement of the Plan hearings that it seems to have occurred to Mr. Garlock that the terms of the agreement could be disregarded and that he might claim the lion's share of any allowance. He has testified to having then warned the firm that it was not doing as much work as he was and that its share of the allowance might, in consequence, be impaired (S.M. 26362). What was the firm to do? Enter into competition with Mr. Garlock at the hearings? That would have been unthinkable and would, besides, not have been tolerated by the District Court. Mr. Garlock had never asked for any specific help that had been refused—at this period he was seeking none. So all the firm could properly do was to send one of its members, Mr. Sidney Struble, to attend the hearings and keep in touch with what was going on. In this way, had Mr. Garlock been disabled, or wanted someone temporarily to replace him, it would have been possible for someone to step into the emergency (S.M. 26745, 26819, 21, *infra*, pp. 14a, 15a). As Mr. Fraenkel testified, he, rather than Mr. Struble, would probably have been the one to do so. (S.M. 26821)—fortunately this never became necessary.

Now Mr. Garlock claims sole credit (as between himself and the firm) for everything accomplished in the Plan hearings. We submit that this is unfair and improper. Many lawyers were representing the interests of the first mortgage bondholders. It would have been absurd and unnecessary duplication for the firm, as well as Mr. Garlock, to have taken an active part in representing the petitioning creditors. But whenever Mr. Garlock wanted help from the firm—and several such occasions arose during the Plan hearings—it was given him (S.M. 26276, 26486-9, 26741, 26832).

It is clear that the firm did a great deal more than, as the court below said, merely holding itself ready to assist Mr. Garlock. In the later stages of the proceeding, when a host of lawyers were appearing representing various interests, it did not seem appropriate for the firm to attempt to rival Mr. Garlock in his endeavors. He was doing an excellent job. For the firm to have insisted on active participation as well would have been unseemly and would have invited criticism for unnecessary duplication. So the firm in that period, in the main, contented itself with having one of its members attend all hearings and with giving Mr. Garlock all the assistance he required.

Nor is the statement correct in the opinion of the court below that a "falling out" occurred between the firm and Mr. Garlock soon after the proceedings started. There was no such falling out until the allowance question arose, years afterward. On the contrary, as the foregoing shows, when differences arose between Messrs. Garlock and Lennox the firm consistently supported Mr. Garlock.

Reasons for Granting the Writ

The decision below raises important questions in the administration of Chapter X which has not been and should be decided by this Court.

It is important that well established law firms be encouraged to participate as attorneys for petitioning creditors in such proceedings. The minuscule compensation here awarded for services performed over a period of eight years is bound to discourage such participation.

It is also important that attorneys associated in the same representation should avoid duplication of services and not compete with each other for the attention of the Court. Yet the decision below has penalized petitioners

for their forbearance from pushing themselves and attempting to displace Mr. Garlock.

This case affords an opportunity for this Court to indicate the extent to which the recommendations of the SEC as to fees should be followed and the grounds which would justify the District Court in disregarding those recommendations.

Finally the statute (11 U. S. C. 641) provides only for payment of compensation to the "attorney" for the petitioning creditors. Petitioners (with Mr. Lennox) were such attorneys; Mr. Garlock was only counsel. The decision below, therefore, ignores the command of the statute.

For all these reasons the petition should be granted.

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